



Memorandum

TO: HONORABLE MAYOR
AND CITY COUNCIL

FROM: Barry Ng
Jennifer A. Maguire

SUBJECT: SEE BELOW

DATE: February 20, 2015

Approved D. D. Sy L

Date 2/20/15

SUBJECT: FIRST AMENDMENT TO TURNER CONSTRUCTION CONTRACT FOR THE UNITED STATES PATENT AND TRADEMARK OFFICE ("USPTO") PROJECT

RECOMMENDATION

- A. Approve the first amendment to the Construction Contract for the United States Patent and Trademark Office Project between the City and Turner Construction, Inc. to do the following:
 - (1) Increase the amount of maximum compensation by \$3,965,110 for a total Maximum Contract Amount not to exceed \$13,601,474; and
 - (2) Set forth a revised construction schedule.
- B. Approve an increase in the amount of the City-controlled project contingency by \$385,081 for a total contingency amount of \$1,348,717.
- C. Adopt the following Appropriation Ordinance and Funding Sources Resolution amendments in the General Fund:
 - (1) Increase the estimate for Revenue from Federal Government by \$3,102,735; and
 - (2) Increase the City-Wide appropriation to the Department of Public Works for the USPTO – Tenant Improvements project by \$3,102,735.

OUTCOME

The recommendation will allow the project to proceed by providing funding for an amended contract with Turner and the issuance of Task Orders. The project is scheduled to be completed by fall 2015.

BACKGROUND

The America Invents Act, signed into law by President Obama in September 2011, called for the USPTO to establish three or more satellite offices. The goal was to improve the speed of the patent application process and draw new talent to the office so that more entrepreneurs can protect their intellectual property in a timely manner, which is critical to attract capital and create jobs.

In January of 2013, the Federal General Services Agency (GSA) launched a search for private office space (35,000-40,000 square feet) in the "delineated area" between San José and Mountain View to lease on behalf of the USPTO. Several San José based building owners expressed interest and the City continued making a strong case that San José uniquely met the GSA's location specifications, which included walking distance to public transit and a variety of restaurants and services nearby.

As noted in the April 15, 2014 Council Memorandum, locating the USPTO in San José has significant public benefits. The City Hall location will provide office space for Patent Examiners and for Patent Trial and Appeal Board (PTAB) Judges. It will include public hearing rooms for PTAB proceedings and a robust patent examiner training facility. In specially designed community outreach space, small businesses and entrepreneurs will be able to learn about USPTO services, meet with patent examiners, and access USPTO's comprehensive search databases. The space will provide public access to search equipment and teleconferencing capabilities.

A. Lease Agreement Between City and USPTO

On July 22, 2014, pursuant to City Council authority delegated on April 15, 2014, a lease agreement was entered between the City and the USPTO for the USPTO to occupy space in the existing City Hall. The lease is based on a project that involves the following two phases: Initial Tenant Improvements and Landlord Alternative Space Improvements.

1. Initial Tenant Improvements

The Initial Tenant Improvements phase of the project involves the City designing and constructing tenant improvements to accommodate the USPTO's lease of approximately 35,200 square feet in the existing City Hall West Wing. Subject to a number of conditions contained in the lease, the USPTO will pay for the design and construction of the Initial Tenant Improvements and will pay a 20.5% management fee to the City.

The lease states that the "preliminary estimate" to design and construct the Initial Tennant Improvements is \$6,500,000 inclusive of a 5% contractor-controlled design-build (DB) contingency. The lease also provides that the cost to design and construct the Initial Tenant Improvements, together with a 10% City/USPTO contingency and a City management fee cannot exceed \$8,700,000 "unless agreed to in writing" by the USPTO. If the USPTO does not agree to pay a higher amount, the USPTO would then be obligated under the lease to reduce the scope of the improvements.

The lease also set forth estimated delivery dates for various floors of the Initial Tenant Improvements. The lease provided that the final schedule would be established through mutual agreement of the parties once agreement is reached with the DB contractor.

2. Landlord Alternative Space Improvements

The Landlord Alternative Space Improvements phase of the project involves the City designing and constructing approximately 50,000 square feet in the existing City Hall Tower and Wing to accommodate staff relocations. The allocation of 35,000 square feet for USPTO space in the Wing created a correspondingly higher relocation footprint due to both fit and program coverage needs. The City is responsible for all initial costs associated with designing and constructing the Landlord Alternative Space Improvements but will be reimbursed by the USPTO over a period of approximately 6 – 7 years via lease revenue payments per the lease agreement. The lease provides that the “preliminary estimate” for designing and constructing the Landlord Alternative Space Improvements is \$4,000,000. The original schematic cost estimate developed by the City was in amount of \$3,136,364.

B. Turner Construction Inc. (DB)

On September 9, 2014, City Council awarded the DB contract for the USPTO Project to Turner Construction Inc. (Turner) for a maximum compensation of \$9,636,364. The maximum compensation consists of \$6,500,000 to design and build the Initial Tenant Improvements and \$3,136,364 to design and build the Landlord Alternative Space Improvements. The City Council also approved a 10% City/USPTO controlled contingency in the amount of \$963,636.

Under the DB agreement, Turner cannot start construction until the parties agree on a Guaranteed Maximum Price (GMP) for constructing the Initial Tenant Improvements and the Landlord Alternative Space Improvements. Turner has now completed the design work needed to construct the various improvements, obtained bids and developed a GMP for the work. The parties have agreed on a design and construction GMP and a schedule for completing the work, both of which require an amendment to the DB contract.

ANALYSIS

A. Increase in Maximum Compensation in Turner Contract

On December 15, 2014, Turner submitted completed plans and specifications for the construction of the Initial Tenant Improvements and the Landlord Alternative Space Improvements that were acceptable to the City and the USPTO. On January 12, 2015, Turner submitted a GMP for constructing both the Initial Tenant Improvements and Landlord Alternative Space. Both the City and USPTO agree with the GMP, and staff is accordingly recommending increasing the maximum compensation in Turner’s DB contract from \$9,636,364 to \$13,601,474.

1. Initial Tenant Improvements

The cost estimate contained in the lease agreement for designing and constructing the Initial Tenant Improvements was based on schematic design plans, which are very general and preliminary. Upon Council award of the Turner contract, the Turner DB team, along with the City's project management team commenced the project's design. The Turner DB team evaluated the schematic design plans prepared by USPTO for the Initial Tenant Improvements.

Once the specific and detailed scope of work for the project was determined, Turner's DB team proceeded to prepare construction documents for bidding and final pricing. During the design review process, both the City and USPTO teams worked closely with the Turner DB team to implement the schematic design concepts with greater accuracy, programmatic and functional requirements.

Final design documents comprised of construction plans and specifications were approved by the City on January 7, 2015. USPTO is in agreement with the final design of its space as reflected in the approved construction plans and specifications.

Based on the approved construction plans and specifications, Turner submitted a total GMP of \$9,545,628 for designing and constructing the Initial Tenant Improvements. This GMP is \$3,045,628 higher than the original estimate. The breakdown between the GMP for design and the GMP for construction is shown in the table below. The increased design and construction costs are mainly:

- Incorporating the latest CA Title 24 requirements.
- First floor design revisions to accommodate better public interface.
- Programming and confidentiality requirements.
- Specific security system requirements.
- Additional HVAC controls in all individual offices.

The following is a summary of the Turner contract costs associated with the Initial Tenant Improvements:

DESCRIPTION	ORIGINAL ESTIMATE	FINAL GMP	DIFFERENCE
Design	\$536,296	\$655,269	\$118,973
Construction	\$5,963,704	\$8,890,359	\$2,926,655
Total Design and Construction	\$6,500,000	\$9,545,628	\$3,045,628

The USPTO has agreed to increase its contribution of the project by \$3,045,628 for their portion of work under the Turner contract. In order to meet the requirements of the lease agreement, the USPTO must provide a written agreement to the increased maximum amount they will be responsible for in connection with the design and construction of the Initial Tenant

Improvements, as well as final delivery dates, prior to final agreement with Turner on the first amendment. The City received the written agreement from USPTO on February 20, 2015.

With regard to the Construction Schedule for the Initial Tenant Improvements, the lease sets forth estimated delivery dates for various floors of the Initial Tenant Improvements. The lease provided that the final schedule would be established through mutual agreement of the parties once agreement is reached with the DB contractor.

The DB contract with Turner sets forth certain estimated dates for beneficial occupancy that were consistent with the dates contained in the lease agreement. The design phase of the project took approximately eight weeks longer than anticipated for a number of different reasons, including the USPTO and City closely evaluating the scope of design, analyzing costs, and strategizing efforts for additional funding, as well as Turner's need to obtain pricing from subcontractors and suppliers.

The City and Turner have agreed to the following revised dates for the USPTO's beneficial occupancy of the various floors:

	Original Schedule in the Lease	Final agreed Schedule
Floor	Acceptance Date (No later Than):	Acceptance Date (No later Than):
First Floor Delivery Date	April 17, 2015	July 16, 2015
Second Floor Delivery Date	August 14, 2015	October 2, 2015
Third Floor Delivery Date	July 10, 2015	September 11, 2015

The first amendment would incorporate the revised schedule into the DB contract. The USPTO has agreed to the revised dates verbally and will include a written agreement as to the dates in the aforementioned written acknowledgement it is preparing.

2. Landlord Alternative Space Improvements

Based on the approved design, Turner submitted a total GMP of \$4,055,846 for designing and constructing the Landlord Alternative Space Improvements. This GMP is \$919,482 higher than the original estimate. The breakdown between the GMP for design and the GMP for construction is shown in the table below. The increased design and construction costs are mainly:

- Additional hard walls and high-density storage for security and confidentiality requirements.
- Programming and design for all impacted departments.

DESCRIPTION	ORIGINAL ESTIMATE	FINAL GMP	DIFFERENCE
Design	\$258,960	\$278,418	\$19,458
Construction	\$2,877,404	\$3,777,428	\$900,024
Total Design and Construction	\$3,136,364	\$4,055,846	\$919,482

The increased amount of \$919,482 has been addressed by an \$850,000 Mid-Year budget adjustment approved by the City Council on February 10, 2015, as well as by City soft costs savings in an amount of \$69,482.

The design for the USPTO will result in the relocation of a number of City departments shown in the table below. While these department relocations will maximize floor space in all floors of the City Hall Tower and Wing, both will be filled to near capacity.

DEPARTMENT	MOVE FROM	MOVE TO
Housing (reconfiguration)	Tower 12	Tower 12
Public Works Events Management	Tower 1	Tower 5
ESD Integrated Billing System	Tower 4	Tower 1 and 7
Code Enforcement (reconfiguration)	Tower 4	Tower 4
Finance (reconfiguration)	Tower 14	Tower 14
S.A.R.A.	Tower 14	Tower 13
OED (OCA and Real Estate)	Tower 14	Tower 12
Police Gaming Unit	Wing 2	Wing 3
Employee Relations	Wing 2	Wing 3
Human Resources	Wing 2	Tower 4
Information Technology (reconfiguration)	Tower 11	Tower 11
City Auditor	Wing 3	Tower 14
City Clerk	Wing 2	Tower 14

With regards to the construction schedule for Landlord Alternative Space Improvements, it is estimated that the City department relocations will begin in early March 2015 and will be completed by mid-June 2015. The Landlord Alternative Space Improvements will need to be coordinated in a manner that enables completion of the Initial Tenant Improvements by the revised USPTO/City construction completion dates.

B. Contingency

The City Council approved a shared 10% contingency between the City and USPTO in the amount of \$963,636. Based on the final GMP for the two project elements as shown in the table below, staff recommends increasing the contingency by \$385,081 to \$1,348,717.

DESCRIPTION	ORIGINAL ESTIMATE	FINAL GMP	DIFFERENCE
Initial Tenant Improvement	\$650,000	\$954,563	\$304,563
Landlord Alternative Space Improvements	\$313,636	\$394,154	\$80,518
Total Contingency	\$963,636	\$1,348,717	\$385,081

C. City Design and Construction Management

The original estimate of the City's cost of its design and construction management services was \$2,565,750. The USPTO lease makes the USPTO responsible for all of the costs of the City's design and construction management services attributable to the Initial Tenant Improvements in the amounts shown below. The City's costs for design and management services have increased due to the increased construction costs. Based on the final GMP, staff recommends an increase to the City's cost of design and management services by \$636,789 to \$3,202,539.

In addition to the \$69,482 soft costs savings discussed in Section A.2 above, additional soft cost savings of \$80,518 are projected and shown as a \$150,000 overall cost reduction in the table below.

DESCRIPTION	ORIGINAL ESTIMATE	FINAL GMP	DIFFERENCE
Initial Tenant Improvement (USPTO)	\$1,365,750	\$2,152,539	\$786,789
Landlord Alternative Space Improvements (City)	\$1,200,000	\$1,050,000	(\$150,000)
Total Design and Construction Management	\$2,565,750	\$3,202,539	\$636,789

The USPTO has agreed to the revised amounts and will include a written agreement as to the amounts in the letter agreement it is preparing.

D. Project Funding

The original project funding provides for a total amount of \$13,165,750. Based on the final GMP, staff recommends an increase of \$4,986,980 for a final total of \$18,152,730. Of the total project funding increase, \$4,136,980 will be for the USPTO's portion of the project and \$850,000 will be for the City's portion. A portion of the additional funding for the USPTO's portion is recommended as part of this memorandum with the remaining portion to be included as part of the 2015-2016 budget process, which all will be fully reimbursed by the USPTO. The additional \$850,000 funding for the City's portion was included as part of the 2014-2015 Mid-Year Budget Review, which was approved by the City Council on February 10, 2015.

DESCRIPTION	ORIGINAL ESTIMATE	FINAL GMP	DIFFERENCE
Total Project Funding	\$13,165,750	\$18,152,730	\$4,986,980

POLICY ALTERNATIVES

Alternative #1: Do not approve cost increase to USPTO.

Pros: City's pay back period generated from revenues will be within 5 years instead of 7 years.

Cons: The current budget does not meet USPTO programming needs and requirements to open their offices in San José.

Reason for not recommending: This alternative is not recommended as it does not support the needs of USPTO to establish its office.

EVALUATION AND FOLLOW-UP

Staff will bring forward recommendations to recognize and appropriate the remaining funding of \$3,433,995, which will be expended and reimbursed in 2015-2016, as part of the 2015-2016 budget process. In the unlikely event that the funds are not appropriated, there is a provision within the contract that allows the City to terminate for convenience. (See Source of Funding below.)

PUBLIC OUTREACH/INTEREST

This item will be posted on the City's website for the March 3, 2015 City Council agenda.

COORDINATION

This staff report has been coordinated with the USPTO, City Attorney's Office, and the Office of Economic Development.

COST SUMMARY/IMPLICATIONS

- 1. AMOUNT OF RECOMMENDATION:** Increase Maximum Design and Construction Costs, including contingency, by \$4,350,191 and increase the USPTO – Tenant Improvement project by \$3,102,735.
- 2. COST ELEMENTS OF AGREEMENT/CONTRACT:**

	City of San José (In 2014-2015)	USPTO (In 2014-2015)	USPTO (In 2015-2016)	Total
Increase Max. Design & Construction Costs				
- DB Contract NTE Amount ⁽¹⁾	\$919,482	\$2,284,221	\$761,407	\$3,965,110
- City/USPTO-Controlled Contingency	\$80,518	\$228,422	\$76,141	\$385,081
Total Increase Max. Design & Construction Costs	\$1,000,000	\$2,512,643	\$837,548	\$4,350,191
City Soft Costs & USPTO Management Fee to the City ⁽²⁾	(\$150,000) ⁽³⁾	\$590,092	\$196,697	\$636,789
Total Increase Project Costs in 2014-2015	\$850,000	\$3,102,735		\$3,952,735
Total Increase Project Costs in 2015-2016			\$1,034,245	\$1,034,245
Total Increase Project Costs	\$850,000⁽⁴⁾	\$3,102,735	\$1,034,245	\$4,986,980

(1) Inclusive of profit, overhead, DB management and DB contingency.

(2) The lease agreement between the City and the USPTO provides for the USPTO to pay a Management Fee to the City for the design and construction management of the USPTO tenant improvements. This Management Fee, which includes a 50% share of the City's DB procurement costs, is capped at 20.5% of the DB contract amount for the USPTO improvements.

(3) The City soft costs are lower by \$150,000 as a result of lower than anticipated Public Works staffing costs.

(4) Additional funding of \$850,000 was approved as part of the 2014-2015 Mid-Year Budget Review.

3. SOURCE OF FUNDING: The total costs associated with the move of the USPTO is \$18,152,730, of which \$5,500,000 is the City's share of the costs related to the relocation of City staff from the City Hall Wing to the City Hall Tower. These costs are funded by the General Fund, and \$200,000 was included as part of the 2013-2014 Mid-Year Budget Review, \$4,450,000 was included as part of the 2014-2015 Adopted Operating Budget, and an additional \$850,000 was included as part of the 2014-2015 Mid-Year Budget Review. The remaining \$12,652,730 is USPTO's share of the costs for tenant improvements, including maximum reimbursable City staff management costs. The City will be the contract manager, and USPTO will reimburse the City for the design, construction, and management costs. It is estimated that \$9,218,735 will be expended and reimbursed in 2014-2015. On September 9, 2014, the City Council approved and appropriated \$6,116,000 for this project, and as part of this memorandum, recommended actions are included to appropriate an additional \$3,102,735 (and recognize the corresponding revenue from the federal government. The remaining \$3,433,995 will be expended and reimbursed in 2015-2016, and budget actions to appropriate and recognize the remaining funds will be included as part of the 2015-2016 budget process. In the unlikely event that the remaining funds are not

appropriated, there is a provision within the contract that allows the City to terminate for convenience.

4. **FISCAL IMPACT:** The USPTO will be responsible for the total design and construction costs associated with its move into the Wing. Lease revenue of approximately \$6.0 million is projected from the USPTO in years one through seven. Over a 20-year period, \$21.5 million in lease revenue is projected. On an ongoing basis, maintenance costs of approximately \$59,000 annually will be incurred by the City's General Fund, which will be incorporated into the 2015-2016 budget process. In the first seven years, the lease revenue from USPTO will be sufficient to offset the relocation costs and maintenance costs. This payback period is longer than the original five-year payback period due to the higher construction costs associated with the City's portion of the project. After the first seven years, and into years 11-20, the lease payments will cover the maintenance costs and generate net revenue. Over a 20-year period, the estimated lease revenue of \$21.5 million is \$14.8 million above the estimated costs of \$6.7 million.

At some time in the future, it may be necessary to lease space outside of City Hall to address any significant growth of City departments. There is sufficient net income from the USPTO lease after year seven to address that situation if necessary, and the opportunity to take back the space for City use after 10 years. The USPTO lease has an initial term of five years. After the five-year term, the USPTO can make one-year lease extensions for 15 years.,

BUDGET REFERENCE

The table below identifies the fund and appropriation proposed to fund the increased costs associated with the USPTO Tenant Improvement project in Year 1, which includes DB construction costs inclusive of DB contingency, City/USPTO contingency, and the City's management fee along with the budget already appropriated for City staff relocation costs and the project.

HONORABLE MAYOR AND CITY COUNCIL

February 20, 2015

Subject: First Amendment to Turner Contract for the USPTO Project

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Fund #	Appn. #	Appn. Name	Total Appn.	Rec. Budget Action	Amount for Amendment	2014-2015 Adopted Capital Budget Page	Last Budget Action (Date, Ord. No.)
Remaining Project Costs (2014-2015 only)			\$14,518,735				
001	3287	United States Patent and Trademark Office – Tenant Improvements	\$6,116,000	\$3,102,735	\$2,512,643	N/A	09/09/2014, Ord. No. 29485
001	7699	United States Patent and Trademark Office – City Staff Relocation	\$5,300,000	N/A	\$1,000,000	V - 1012	02/10/2015, Ord. No. 29533
Total Current Funding Available			\$11,416,000				
New Funding to be Appropriated				\$3,102,735			
TOTAL FUNDING				\$14,518,735			
001	R110	Revenue from Federal Government	\$11,466,924	\$3,102,735	N/A	N/A	02/10/2015, Ord. No. 77282

CEQA

Exempt, File No. PP14-031.

/s/

BARRY NG

Interim Director of Public Works



JENNIFER A. MAGUIRE

Interim Senior Deputy City Manager /
Budget Director

I hereby certify that there will be available for appropriation in the General Fund in the Fiscal Year 2014-2015 moneys in excess of those heretofore appropriated therefrom, said excess being at least \$3,102,735.



JENNIFER A. MAGUIRE

Interim Senior Deputy City Manager /
Budget Director

For questions, please contact Barry Ng, Interim Director of Public Works, at 408-535-8477.